TAB D

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

In the Matter of		
Qwest Communications International Inc.	)	WC Docket No. 02-189
Consolidated Application for Authority to Provide In-Region, InterLATA Services in Montana, Utah, Washington and Wyoming	)	

DECLARATION OF STEVE BICKLEY ON BEHALF OF AT&T CORP.

Based on my personal knowledge and on information learned in the course of my duties, I, Steven P. Bickley, declare as follows:

1. My name is Steven P. Bickley. I am Vice President of Finance for the CFO division of AT&T Consumer. I am responsible for financial planning, operational and business analysis for AT&T's local operations. As part of my job, I evaluate and review AT&T's internal costs to offer local telephone service in order to evaluate the financial viability of providing residential local service in markets that AT&T has not yet entered. The purpose of this declaration is to demonstrate why, based on recent cost analyses, AT&T requires at least a $10 margin beyond connectivity costs to enter the UNE-P local market in Montana, Utah, and Washington.

2. Based upon AT&T's actual experience in providing residential UNE-P based service to more than one million customers in New York, Texas, Michigan, Georgia, Illinois and Ohio, supplemented by an analysis of areas in which further cost reductions may be possible with greater scale and experience, a gross margin between total local revenues and connectivity costs paid to the incumbent of at least $10 is

required for an efficient competitive carrier to cover its internal retailing and related costs. This $10 figure does not reflect AT&T's average costs per line today, which are significantly higher, but is instead a target "benchmark" of the best that a competitive carrier like AT&T could hope for in a competitive environment. As AT&T's experience confirms, the reality is that a new market entrant is likely to incur higher costs, at least initially (and possibly for a substantial period of time) in competing in a new line of business against an entrenched monopoly provider. Thus, based upon my experience and analysis, AT&T will incur *at least* $10 in internal costs per line per month even taking into account the possible economies of scale, efficiencies, and savings of a large and efficient, market competitor.

3. Much of these internal costs are costs over which AT&T has little discretion. Notably, the costs that I identify below do *not* include any start-up costs of creating an infrastructure to provide local service, nor do they include any economic profit to AT&T. The quite substantial start-up costs that are omitted from this analysis include, among others, the development of systems to interconnect with the ILEC's OSS systems, external billing mechanisms, the training of customer care representatives for the entry state, and systems readiness testing.

4. The remaining sections of this declaration review the internal costs that an efficient new entrant would have to recover when entering local telephone markets in Montana, Utah, and Washington.

MONTANA

5. First, AT&T expects to incur average local customer care costs of at least *** *** per line per month. This figure includes the costs of answering customers'

questions about their service, providing trouble support when customers report service problems, and performing account maintenance functions. This figure was estimated by analyzing current costs and reducing those costs by a *** *** factor to account for productivity improvements. These costs are primarily a function of normal customer activity. However, these costs may significantly increase if an incumbent provides poor OSS support for AT&T's local service provided via UNE-P. AT&T's actual local customer care costs are higher than this figure.

6. Second, AT&T incurs uncollectible expenses when customers do not pay their bills. AT&T's multi-state experience is that about *** *** of local service revenue is uncollected when customers do not pay their bills. Applying that factor to AT&T's expected average revenues for Montana of approximately $29.53 per line per month generates an expected uncollectible expense of at least *** *** per month per line. There is little a competitive carrier can do to reduce this basic cost of doing business.

7. Any local service provider also incurs costs for billing and collections. A conservative estimate of expected billing and collection costs is approximately *** *** per month per line. This figure, which is lower than AT&T's current actual costs, is based upon analysis of AT&T's current costs and reducing those costs by a *** *** factor to account for productivity improvements, and includes the cost of collecting and collating customer billing information, preparing and sending out initial bills, sending letters to customers who do not pay, and associated collection activities.

8. Based upon AT&T's experience in New York, Texas, Michigan, Georgia, Illinois and Ohio, efficient, forward looking marketing and sales cost to acquire and

provision a local telephone customer are, on average, at least *** *** per line. This figure includes advertising, promotions, telemarketing, other marketing channel costs, as well as the cost of ordering and provisioning. This figure is again lower than AT&T's actual costs today and reflects a *** *** factor to account for future productivity improvements. Amortizing this expense over a reasonable customer retention period generates an average monthly cost of *** ***.

9. Finally, a local service provider can expect to incur modest other General & Administrative costs of approximately *** *** per month per line. These costs include incremental product and market management, systems maintenance costs and other network related expenses associated with a local marketplace offer. These costs are estimated by analyzing current costs and reducing those costs by a *** *** factor to account for productivity improvements.

10. The sum of these foreseeable and unavoidable monthly internal costs is *** ***. As noted above, this figure does not include all monthly internal costs, particularly start up expenses, and is based upon benchmark targets that reflect predicted cost savings that go well beyond actual experience.

11. These internal costs are for "UNE-P" service. The internal costs in connection with resale local service would not be materially different. The types of costs included here are primarily customer and market facing costs that must be incurred regardless of entry method. If AT&T were to support both entry platforms at once, AT&T's internal costs would remain equivalent or likely increase in view of the additional incremental costs for systems and marketing programs to accommodate both platforms.

UTAH

12. First, AT&T expects to incur average local customer care costs of at least *** *** per line per month. This figure includes the costs of answering customers' questions about their service, providing trouble support when customers report service problems, and performing account maintenance functions. This figure was estimated by analyzing current costs and reducing those costs by a *** *** factor to account for productivity improvements. These costs are primarily a function of normal customer activity. However, these costs may significantly increase if an incumbent provides poor OSS support for AT&T's local service provided via UNE-P. AT&T's actual local customer care costs are higher than this figure.

13. Second, AT&T incurs uncollectible expenses when customers do not pay their bills. AT&T's multi-state experience, is that about *** *** of local service revenue is uncollected when customers do not pay their bills. Applying that factor to AT&T's expected average revenues for Utah of approximately $27.31 per line per month generates an expected uncollectible expense of at least *** *** per month per line. There is little a competitive carrier can do to reduce this basic cost of doing business.

14. Any local service provider also incurs costs for billing and collections. A conservative estimate of expected billing and collection costs is approximately *** *** per month per line. This figure, which is lower than AT&T's current actual costs, is based upon analysis of AT&T's current costs and reducing those costs by a *** *** factor to account for productivity improvements, and includes the cost of collecting and collating customer billing information, preparing and sending out initial bills, sending letters to customers who do not pay, and associated collection activities.

15. Based upon AT&T's experience in New York, Texas, Michigan, Georgia, Illinois and Ohio, efficient, forward looking marketing and sales cost to acquire and provision a local telephone customer are, on average, at least *** *** per line. This figure includes advertising, promotions, telemarketing, other marketing channel costs, as well as the cost of ordering and provisioning. This figure is again lower than AT&T's actual costs today and reflects a *** *** factor to account for future productivity improvements. Amortizing this expense over a reasonable customer retention period generates an average monthly cost of *** ***.

16. Finally, a local service provider can expect to incur modest other General & Administrative costs of approximately *** *** per month per line. These costs include incremental product and market management, systems maintenance costs and other network related expenses associated with a local marketplace offer. These costs are estimated by analyzing current costs and reducing those costs by a *** *** factor to account for productivity improvements.

17. The sum of these foreseeable and unavoidable monthly internal costs is *** ***. As noted above, this figure does not include all monthly internal costs, particularly start up expenses, and is based upon benchmark targets that reflect predicted cost savings that go well beyond actual experience.

18. These internal costs are for "UNE-P" service. The internal costs in connection with resale local service would not be materially different. The types of costs included here are primarily customer and market facing costs that must be incurred regardless of entry method. If AT&T were to support both entry platforms at once, AT&T's internal costs would remain equivalent or likely increase in view of the

additional incremental costs for systems and marketing programs to accommodate both platforms.

WASHINGTON

19. First, AT&T expects to incur average local customer care costs of at least *** *** per line per month. This figure includes the costs of answering customers' questions about their service, providing trouble support when customers report service problems, and performing account maintenance functions. This figure was estimated by analyzing current costs and reducing those costs by a *** *** factor to account for productivity improvements. These costs are primarily a function of normal customer activity. However, these costs may significantly increase if an incumbent provides poor OSS support for AT&T's local service provided via UNE-P. AT&T's actual local customer care costs are higher than this figure.

20. Second, AT&T incurs uncollectible expenses when customers do not pay their bills. AT&T's multi-state experience is that about *** *** of local service revenue is uncollected when customers do not pay their bills. Applying that factor to AT&T's expected average revenues for North Dakota of approximately $24.71 per line per month generates an expected uncollectible expense of at least *** *** per month per line. There is little a competitive carrier can do to reduce this basic cost of doing business.

21. Any local service provider also incurs costs for billing and collections. A conservative estimate of expected billing and collection costs is approximately *** *** per month per line. This figure, which is lower than AT&T's current actual costs, is based upon analysis of AT&T's current costs and reducing those costs by a *** ***

factor to account for productivity improvements, and includes the cost of collecting and collating customer billing information, preparing and sending out initial bills, sending letters to customers who do not pay, and associated collection activities.

22. Based upon AT&T's experience in New York, Texas, Michigan, Georgia, Illinois and Ohio, efficient, forward looking marketing and sales cost to acquire and provision a local telephone customer are, on average, at least *** *** per line. This figure includes advertising, promotions, telemarketing, other marketing channel costs, as well as the cost of ordering and provisioning. This figure is again lower than AT&T's actual costs today and reflects a *** *** factor to account for future productivity improvements. Amortizing this expense over a reasonable customer retention period generates an average monthly cost of *** ***.

23. Finally, a local service provider can expect to incur modest other General & Administrative costs of approximately *** *** per month per line. These costs include incremental product and market management, systems maintenance costs and other network related expenses associated with a local marketplace offer. These costs are estimated by analyzing current costs and reducing those costs by a *** *** factor to account for productivity improvements.

24. The sum of these foreseeable and unavoidable monthly internal costs is *** ***. As noted above, this figure does not include all monthly internal costs, particularly start up expenses, and is based upon benchmark targets that reflect predicted cost savings that go well beyond actual experience.

25. These internal costs are for "UNE-P" service. The internal costs in connection with resale local service would not be materially different. The types of costs

included here are primarily customer and market facing costs that must be incurred regardless of entry method. If AT&T were to support both entry platforms at once, AT&T's internal costs would remain equivalent or likely increase in view of the additional incremental costs for systems and marketing programs to accommodate both platforms.

33. This concludes my declaration on behalf of AT&T.

VERIFICATION PAGE

I, Steven P. Bickley, declare under penalty of perjury that the foregoing is true and correct.

/s/ Steven P. Bickley
Steven P. Bickley

August 1, 2002

TAB E

Before the
Federal Communications Commission
Washington, DC 20554

In the Matter of	)	
Qwest Communications International Inc., Consolidated Application for Authority to Provide In-Region, InterLATA Services in Montana, Utah, Washington and Wyoming	)	WC Docket No. 02-189

JOINT DECLARATION OF DEAN FASSETT AND ROBERT MERCER ON BEHALF OF AT&T CORP.

I. BACKGROUND AND QUALIFICATIONS.

1. **Dean Fassett.** My name is Dean Fassett. I am the owner of Adirondack Telecom Associates, a consulting firm that provides expert engineering, economic modeling, and other technical assistance to telecommunications companies. My current address is 141 Juniper Drive, Ballston Spa, New York, 12020.

2. I graduated from the State University of New York at Cobleskill in 1967 with an AAS degree. From 1970 through 1996 I worked at New York Telephone (NYNEX), where I held positions as an Outside Plant Engineer, an Engineering Manager, and as an Area Construction/Engineering Operations Manager. In that capacity, I oversaw outside plant construction for the Adirondack District, covering 43 wire centers with a customer base of approximately 188,000 access lines. I supervised 14 first level management and 71 craft personnel responsible for designing and building outside plant facilities.

3. In 1996, I joined Frontier Communications of Ausable Valley, as a Contract Outside Plant Engineer and Construction Coordinator. In 1998 I joined Frontier Communications of Ausable Valley as a full time Contract Operations Manager and Engineer, where I was responsible for all aspects of company operations within my service area. In 1996, I founded Adirondack Telecom Associates, where I have worked as a consultant providing expert advice and analysis to telecommunications firms throughout the country.

4. I have provided outside plant local loop expert advice to AT&T and MCI relating the development of the HAI Model. I also have testified in 14 state jurisdictions on behalf of AT&T and MCI as an expert outside plant engineer and construction witness.

5. **Robert Mercer.** My name is Robert A. Mercer. I am the President of BroadView Telecommunications, LLC ("BVT"), a consulting firm specializing in analyses of the telecommunications infrastructure. The address of the firm is 5201 Holmes Place, Boulder, Colorado, 80303.

6. I received a Bachelor of Science degree in Physics from Carnegie Institute of Technology (now Carnegie - Mellon University) in 1964, and a Ph.D. in Physics from Johns Hopkins University in 1969. After receiving my Ph.D., I was an Assistant Professor of Physics at Indiana University from 1970 until 1973.

7. I then joined Bell Telephone Laboratories. Over the next eleven years, I held a variety of positions in the Network Planning organizations at Bell Labs and AT&T General Departments. My final position at Bell Labs was Director of the Network Architecture Planning Center, where I managed an organization that was responsible for early Bell System planning of

the Integrated Services Digital Network (ISDN), as well as systems engineering for new data services being planned by AT&T.

8. I joined Bell Communications Research (Bellcore, now Telcordia Technologies) in January, 1984, where I was Assistant Vice President of Network Compatibility Planning. Among other responsibilities, I directed Bellcore's technology analysis of various legal and regulatory proceedings at the federal and state levels. I also coordinated and provided direction to Bellcore's activities in domestic and international standards activities, and served as a member of the Board of Directors of the American National Standards Institute.

9. After leaving Bellcore in late 1985, I held positions with BDM Corporation and AT&T Bell Laboratories before joining Hatfield Associates, Inc., in early 1987. I held the positions of Senior Consultant, Senior Vice President, and President of the firm. On October 1, 1997, the former principals and employees of Hatfield Associates, Inc., formed HAI Consulting, Inc., and I became the President of that firm. At Hatfield Associates and HAI, I was extensively involved in the development of the various versions of the HAI Model. I also presented testimony on and defended the model in a large number of regulatory proceedings pertaining to the cost of Unbundled Network Elements and Universal Service.

10. In March of 2000, I left HAI to form BroadView Telecommunications. The firm provides strategic planning, education, and expert services related to public and private telecommunications infrastructure, dealing specifically with network architectures, technologies, services, and service providers. At BroadView, I have continued to present and defend the HAI Model in numerous regulatory proceedings, as well as working with HAI to further evolve the HAI Model as appropriate.

11. I also hold an adjunct faculty position in the Interdisciplinary Telecommunications Program at the University of Colorado in Boulder, where I am developing an executive seminar on telecommunications developments, teach a course on telecommunications technology, and serve on Masters thesis committees. I have previously taught a course on advanced data communications and computer networking for several years. I have taught many other courses and seminars as well for other organizations and institutions, in the areas of the telecommunications infrastructure, network technologies, broadband networks, data and voice communications, computer networking, and network management.

II. PURPOSE AND SUMMARY.

12. The purpose of our testimony is to demonstrate that the unbundled network element ("UNE") loop rates adopted by the state Commission's in Washington, Wyoming, Utah and Montana are substantially inflated by clear TELRIC errors. In Parts III through VI of this declaration, we summarize the Washington, Wyoming Utah and Montana UNE rate proceedings that resulted in Qwest's SGATs. We demonstrate that the methodologies employed by those state commissions to develop Qwest's UNE loop rates are inflated by numerous clear TELRIC errors.

III. QWEST'S WASHINGTON UNE LOOP RATES ARE INFLATED BY CLEAR TELRIC ERRORS.

13. The recurring loop rates adopted by the Washington Utilities and Telecommunications Commission ("WUTC") are not TELRIC-compliant. The rates adopted by the WUTC are the result of two separate pricing proceedings ("Phases"). In Phase I, the WUTC purported to determined Qwest's (then US WEST's) and Verizon's (then GTE's) forward-

looking recurring loop costs, net of common costs.[1] In Phase II, the WUTC adopted a "common cost factor" to increase the recurring and loop and switching costs developed in Phase I in order to account for the common costs associated with those elements. In the Phase II proceeding, the WUTC adopted recurring loop rates for Qwest (and for Verizon) equal to the Phase I costs grossed up by the common cost factor adopted in Phase II.[2]

14. The WUTC committed numerous clear errors in both Phase I and in Phase II that vastly inflate the recurring loop rates that would be produced by any reasonable application of TELRIC-principles. Even Qwest appears to recognize that these inflated recurring rates would not pass muster at this Commission and has, at the last minute (about a month before filing its Section 271 Application), unilaterally lowered those rates in order to "expedite consideration of Qwest's Section 271 application." *See* Thompson Decl. ¶ 9. Qwest claims that these eleventh hour rates reductions result in TELRIC rates simply because the new rates are lower than the rates adopted by the WUTC. This argument does not withstand scrutiny, because Qwest's initial rates are not remotely TELRIC-compliant, and because Qwest has made no effort to arrive at new rates based on any semblance of a TELRIC study. Arbitrarily reducing rates no more guarantees TELRIC compliance than does the non-compliant process by which the rates were set in the first place.

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[1] *See* Eighth Supplemental Order, Interim Order Establishing Costs for Determining Prices in Phase II; And Notice of Prehearing Conference, *Pricing Proceeding for Interconnection, Unbundled Elements, Transport and Termination, and Resale*, Docket Nos. UT-960369, -960370, -960371 (May 11, 1998) ("*Phase I Order*").

[2] *See* 17th Supplemental Order, Interim Order Determining Prices; Notice of Prehearing Conference, *Pricing Proceeding for Interconnection, Unbundled Elements, Transport and Termination, and Resale*, Docket Nos. UT-960369, -960370, -960371 (September 23, 1999) ("*Phase II Order*").

15. As noted above, the recurring loop rates adopted by the WUTC are the product of a two-phase proceeding. In Phase I, the WUTC adopted costs for those rate elements net of common costs. In Phase II, the WUTC made a few changes to the costs developed in Phase I, adopted common cost factors, and adopted final recurring loop rates. As demonstrated below the methodologies used by the WUTC to develop Qwest's Washington recurring loop rates in these proceedings were not remotely TELRIC-compliant.

16. *Phase I.* The WUTC's purported purpose for the Phase I proceeding was "to develop an appropriate and consistent cost methodology with which to determine the costs of providing certain telecommunications services." *See Phase I Order* at 2. Three cost models were presented to the WUTC: (1) Sprint submitted the Benchmark Cost Proxy Model ("BCPM"); (2) Qwest submitted its Regional Loop Cost Analysis Program ("RLCAP"); and (3) AT&T submitted the Hatfield Model (the Hatfield Model is now called the "HAI Model"). *See Phase I Order* ¶ 13. The WUTC adopted none of these cost models to develop recurring loop and switching rates, finding that "none of the models satisfies the [WUTC's] . . . objective of being open, reliable, and economically sound." *Phase I Order* ¶ 38. The WUTC emphasized that the RLCAP cost study "is inflexible, closed, and uses inputs for buried cable and utilization rates that are inconsistent with its actual operations" and that the "BCPM inputs are based upon a proprietary study of LEC operations, thus violating the [WUTC] . . . requirement for the use of open models, its use of per line expenses for outside plant is not economically sound, and it has at least one algorithmic error." *Phase I Order* ¶ 264.

17. There is no question that the BCPM and RLCAP cost studies contained numerous clear TELRIC errors. With respect to the BCPM, even the WUTC was troubled by the model's assumptions: "we find it troublesome the method used to develop the BCPM inputs. The input

values are based on a proprietary survey that was not made available to other parties. Furthermore, the mix of activities is based on the opinion of an industry group." *Phase I Order* ¶ 83.

18. The fact that the BCPM is not TELRIC-compliant should come as no surprise to this Commission. Indeed, the Commission has in the past expressly rejected the underlying methodology employed by the BCPM to calculate loop costs, as well as many of the default inputs used in that model. In the *Platform Order*, 13 FCC Rcd. 21323 (1998), this Commission found that the HAI model's approach for determining how to "group and serve . . . customers in an efficient and technologically reasonable manner" was superior to BCPM's "simplist[ic]" approach that "generat[e]d artificial costs." *Id.* ¶ 46. In particular, the Commission found BCPM's methodology *flawed* because it would "require separate facilities to serve customers that are [in fact] in close proximity." *Id.* Similarly, in determining what approach should be used to "design" the outside plant, the Commission found that the BCPM, unlike the HAI model, did not "adhere to sound engineering and forward-looking, cost-minimizing principles." *Id.*¶ 54. Thus, the Commission found that BCPM did not use proper "optimization routines through use of sound network engineering design to use the most cost-effective forward-looking technology." *Id.* ¶ 61.

19. The Commission in its *Platform Order* and subsequent *Inputs Order*, 14 FCC Rcd. 20156 (1999), also rejected many of the key inputs used in the BCPM. For example, the Commission found that BCPM overstated costs by assuming that "loop lengths that exceed 12,000 feet will be fiber cables." *Platform Order* ¶¶ 68, 70. The Commission also has found the BCPM "assum[ption] that an efficient telephone company will benefit only marginally from sharing" is contrary to TELRIC principles. *Id. Inputs Order* ¶¶ 242, 243. And the Commission

rejected the cable cost per input values supported by BCPM's sponsors, which were based on cable costs reported by the incumbent LECs, in favor of the publicly available data provided and supported by AT&T and the HAI sponsors. *Id.* ¶¶ 103, 105.

20. Qwest's RLCAP model also contains fundamental TELRIC errors that inflate loop costs. As summarized in the Report of the Administrative Law Judge in the Minnesota Generic UNE Cost Proceeding:[3]

- RLCAP, "like all the U S WEST models, . . . heavily rely on embedded costs and structures and assumptions based on old data;"
- RLCAP "does not actually model any distribution areas or compute costs based on information about the distribution areas in which actual customer locations are found, [and] neither provides nor uses any information about distribution area boundaries or distribution area living units;"
- RLCAP "does not attempt to model either actual or forward-looking distribution lengths in the 'scorched node' context required for a TELRIC analysis;"
- RLCAP uses "loop length data from several sources, [and] [o]f the various potential data sources mentioned, the documentation does not reveal which sources were actually used;
- RLCAP makes a number of illegitimate assumptions about the density group constituents of each grouping of wire centers, by, for instance, using the same density group assumptions across all 14 of its states;
- RLCAP "does not attempt to estimate costs for specific distribution areas," whereas "HAI constructs clusters based on actual locations of customers in Minnesota and then develops distribution costs based on the location of the cluster and its distance from the wire center;"
- RLCAP "makes no use of geocoded data to locate customers; [n]or do RLCAP's distribution area designs rely on census data; rather, [t]he distribution designs were developed by several U S WEST engineers in 1988, [and] U S WEST has not provided any other support for these designs;"

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[3] *In the Matter of a Generic Investigation of U S West Communications, Inc.'s Cost of Providing Interconnection and Unbundled Network Elements*, OAH Docket No. 12-2500-10956-2, MPUC Docket No. P-442, 5231, 3167, 466, 421/C1-96-1540, Report of the Administrative Law Judge, November 17, 1998, starting at ¶16.

- Whereas "[c]orrect estimates of costs should have the numerator (the total increment of costs required to provide the element of concern) consistent with the denominator (the demand for the element to be provided with those facilities)," U S WEST "does not have a proper match of the numerator and denominator;"

- RLCAP's density group design approach "artificially limits the economies of scale potentially achievable in a scorched node environment," by failing to " permit the deployment of any equipment that is available provided that such equipment is least-cost and embodies forward-looking technology;" and

- U S WEST does not make consistent structure sharing assumptions between states, because, for instance, in Minnesota, "RLCAP assumes that developers will pay 20% of the costs of placing buried cable facilities in distribution areas and that when developers do not pay such costs, it will incur 100% of such placement costs," whereas in Oregon, "U S WEST signed a Stipulation with OPUC Staff in which it agreed that it was reasonable to assume developers would pay 35% of the placement costs for buried cables."

21. Based on these and other identified weaknesses, the judge concluded "RLCAP does not qualify for serious consideration in this proceeding. It has not been shown to produce reliable, reasonable results. It cannot be used to calculate geographically deaveraged rates in a meaningful way. None of its major defects can be remedied easily. RLCAP is an unacceptable model for the purpose of determining UNE costs for U S WEST in Minnesota."

22. Although much more succinct in his comments, the ALJ in Arizona found, and the Arizona Corporation Commission adopted, a similar finding with respect to U S WEST's LoopMod, the successor program to RLCAP: "Qwest's model is based primarily upon its embedded network and costs," and it "fails to adequately incorporate efficiencies that should be recognized in a TELRIC environment."[4]

[4] *In the Matter of the Investigation into Qwest Corporation's Compliance with Certain Wholesale Pricing Requirements for Unbundled Network Elements and Resale Discounts*, Arizona Corporation Commission Docket T-00000A-00-0194, Phase II Opinion and Order, June 12, 2002, p. 10 (emphasis added).

23. Furthermore, both the BCPM and RLCAP cost models submitted in the Washington pricing proceedings are based on very stale data. Those cost studies generally rely on pre-1997 data. But efficiencies in the telecommunications industry combined with efficiencies enjoyed by Qwest given its post-1997 mergers have led to dramatically lower loop costs.

24. Rather than working with the parties to develop TELRIC-compliant cost studies, the WUTC changed some of the inputs in each of the cost studies, re-computed loop rates based on each of those adjusted cost studies, and "averaged" those costs to obtain what the WUTC termed a "cost floor[]" for loop rates. *See Phase I Order* ¶ 265. The WUTC's conclusion that its methodology created a TELRIC loop cost floor is nonesense. The WUTC conceded that the changes that it made to each cost study did not address the numerous TELRIC-errors in those cost studies. *See Phase I Order* ¶ 269 ("we could not modify the models to comport to our findings . . . in those cases we simply note the likely [directional] impact on the loop cost"). Thus, to the extent that the clear TELRIC errors that were not addressed by the WUTC overstated loop Qwest's Washington loop rates, the average of the cost models containing those errors results in loop rates that substantially exceed that which any reasonable application of TELRIC principles would have produced.

25. Even worse, the WUTC's "averaging" process is completely unexplained, and further overstates Qwest's Washington loop rates. After adjusting each of the cost studies to correct for some (but not all, as the WUTC conceded) of the clear TELRIC errors in those cost studies, the WUTC determined that the Hatfield, BCPM, and RLCAP cost models produced per-line monthly recurring loop costs of $13.53, $17.23, and $13.76. Based on these results, the WUTC determined that the "cost of the unbundled loop [for Qwest in Washington] is $17.00,"

Phase I Order ¶ 269, which is almost the same cost produced by the defective BCPM. The WUTC's "average" is more than $2.00 higher than the simple average ($14.84) produced by the three cost models that the WUTC itself determined produce non-TELRIC loop costs. To date, the WUTC has never explained how, based on the rates produced by the three adjusted cost studies, it calculated a $17.00 loop rate. And AT&T has never been able to reproduce that loop rate, nor has any other party demonstrated the ability to reproduce that rate. The black-box characteristics of the loop rates adopted by the WUTC are, ironically, at odds with the reasoning provided by the WUTC for not adopting any one of the three cost studies supported by the parties – that "those cost models were not open, and did not provide[] all parties an opportunity to fully explore the advantages and the limitations of the difference cost models." *Phase I Order* ¶ 24.

26. Four months later, the WUTC further adjusted the BCPM to account for deferred taxes.[5] That change reduced the loop costs produced by the BCPM from $17.23 to $15.72. *See id.* ¶ 3. After making this change, the WUTC reported that the Hatfield, BCPM and RLCAP cost models produce loop cost estimates of $13.53, $15.72, and $13.76, respectively. The WUTC then asserted, with no explanation, that the "evidence in the record" supports a finding that "the cost of the unbundled loop is $16.25," *id.* ¶ 14, which is substantially *higher* than the loop cost produced by any of the three cost models. Not surprisingly, AT&T could not reproduce the WUTC's findings based on the record in that proceeding.

[5] *See* Fourteenth Supplemental Order, Prehearing Conference Order Resolving Technical Issues, *Pricing Proceeding for Interconnection, Unbundled Elements, Transport and Termination, and Resale*, Docket Nos. UT-960369, -960370, -960371 (September 30, 1998) ("*14th Supp. Order*").

27. About one year later, the WUTC released its *Phase II Order*, wherein the WUTC adopted UNE loop rates, based on the costs approved in the *Phase I* proceeding and the *14th Supp. Order*. In the *Phase II Order,* the WUTC produced a table summarizing its purported findings in the *Phase I Order*. *Phase II Order* ¶ 205. The WUTC confirmed that the Hatfield, BCPM and RLCAP cost models produce loop cost estimates of $13.53, $15.72, and $13.76, respectively. *See id.* However, the table also included a line titled "Commission [WUTC] Adjustment per 8th ORDER [*Phase I Order*]." *Id.* Those adjustments increased the cost estimates produced by the Hatfield, BCPM and RLCAP cost models by $2.31, $0.75, and $2.68, respectively. *See id.* In fact, however, those adjustments were not adopted in the *Phase I Order* – indeed, the *Phase I Order* explicitly states that the WUTC made no such adjustment, and in fact was not able to make such quantitative adjustments. Rather, those adjustments appeared *for the first time* in the *Phase II Order*. To this day, the WUTC has not explained how it computed those adjustments, when it computed those adjustments, or what exactly those adjustments represent. Nor has any party been offered an opportunity to rebut those black-box "adjustments."

28. In reality, the loop cost adjustments listed in the WUTC's *Phase II Order* appear to be a *post hoc* justification for the $16.25 loop cost adopted by the WUTC in the *14th Supp. Order*. Indeed, after adding those unexplained cost adjustments to the loop costs adopted by the Commission in the *14th Supp. Order* the cost estimates produced by the Hatfield, BCPM and RLCAP cost models are $15.84, $16.47, and $16.44, respectively. And the average of these values is $16.25. Thus, it appears that the WUTC's adjustments are nothing more than an eleventh hour attempt to justify its adoption of a $16.25 loop cost for Qwest. On this record, there can be no finding that the WUTC applied TELRIC-compliant principles to develop

Qwest's loop cost – indeed, it is impossible to determine what (if any) pricing principles the WUTC used to develop those costs.[6]

29. We also understand that federal courts have stated that that crude averaging of rates from various non-TELRIC cost studies – whatever averaging process is used – cannot result in TELRIC-based rates. *AT&T Communications of New Jersey, Inc. v. Bell Atlantic-New Jersey*, Civ. No. 97-5762 (KSH), slip op. (D.N.J. June 6, 2000). There, New Jersey BPU was faced with two competing cost models – AT&T's HAI model and Bell Atlantic's proprietary cost model. *Id.* at 28-29. Although the New Jersey BPU found that Bell Atlantic's model did not follow TELRIC, like the WUTC, it questioned the way in which the HAI model calculated outside plant. Decision and Order, Docket No. TX 951205631 (N.J. BPU Dec. 2, 1997). And like the WUTC, having found all models "flawed," the Board simply cast aside the controlling legal standards – and its own assessment of the parties' proposed cost models – in favor of a crude "compromise" and took an average of the two cost models. *AT&T Communications*, slip op. at 27-29.

30. In reversing the New Jersey BPU's order, the court expressly rejected the Board's contention that the resulting rates were TELRIC compliant because, by averaging the two models, it balanced out the "flaw[s]" in the models. *Id.* Rather, the Court found that averaging the results of an embedded and forward-looking cost model resulted in "no real or tangible cost calculation at all." *Id.* at 29. The Court also observed that the Board's baby-splitting was

[6] According to the WUTC, the $16.25 loop cost adopted by the WUTC did not reflect common costs. Thus, to develop UNE loop rates the WUTC adopted a common cost additive for each of the three cost models. The WUTC then adopted rates based on the average of the costs (including the common cost additive) of the three cost studies. Based on this analysis, the WUTC ultimately adopted a loop rate for Qwest for $18.16.

logically flawed because the "averaging" was "applied evenly to all elements collectively" when, as here, the flaws in the various cost models affected rate elements differently. *Id.* at 28.

31. On this record, there is no basis on which this Commission can find that the loop costs adopted by the WUTC in the Phase I proceeding are TELRIC-compliant.

IV. QWEST'S UTAH UNE LOOP RATES ARE INFLATED BY CLEAR TELRIC ERRORS.

32. Qwest effectively acknowledges that the UNE loop rates actually set by the Utah PSC are not remotely TELRIC-compliant. Instead of relying on those rates, Qwest has filed "new" UNE rates, based on a "benchmarking" analysis of the rates set in Utah. In their accompanying Declaration, Messrs. Lieberman and Pitkin explain why these new rates cannot be considered TELRIC-compliant because the benchmarking analysis used by Qwest is flawed. But there is also an additional reason why Qwest's eleventh hour rate reductions should not be considered with respect to Utah. Despite filing the "new" rates that it claims are TELRIC-compliant, Qwest continues to advocate substantially higher rates in the Utah PSC's ongoing UNE rate proceeding. Thus, it is clear that Qwest's gambit is to get its section 271 application approved on the basis of its current rates (lowered only shortly before its Section 271 Application, and not justified on the basis of any TELRIC-compliant model it identified) and then subsequently have those rates hiked to competition-foreclosing levels.

33. For these reasons, Qwest's application must ultimately must be measured by the rates set by the Utah PSC. And there can be no doubt that the rates the PSC set for loops are inflated by clear TELRIC errors. Qwest's loop and switching UNE rates were set by the Utah PSC in 1999 on the basis of 1998 cost data. *See* Report and Order, Docket No. 94-999-01 (Utah PSC June 10, 1999) ("*1999 Utah UNE Pricing Order*"). Given that the costs of providing UNEs

have declined considerably in since this time, these stale UNE rates cannot be considered to be representative of the forward-looking, economic costs of providing UNEs today.

34. But even judged on the basis of 1998 costs, the rates set by the 1999 Utah UNE Pricing Order must be considered excessive. In setting loop and switching rates, the Utah PSC "split the baby," taking the average of AT&T's and US WEST's proposed rates. Although this resulted in rates that were somewhat lower than advocated by US WEST, the resulting rates were still excessive.

35. In particular, in its *1999 Utah UNE Pricing Order*, the Utah PSC found that US WEST's cost model did not satisfy the Commission's TELRIC methodology. As the Utah PSC correctly observed, the ICM "does not produce a forward-looking, economically efficient network" but instead "mimics the embedded costs of recent network experience." *1999 Utah UNE Pricing Order* at 6-7. Thus, the Utah PSC concluded that the ICM resulted in rates that were overstated. *Id.* at 7.

36. This conclusion was well-founded. The ICM uses a component called LoopMod to calculate loop investments. LoopMod is the U S WEST's successor to RLCAP. We have already noted that the Arizona Corporation Commission found LoopMod to be defective for the same reasons in summary that RLCAP is: it is largely based on embedded costs, and it fails to incorporate efficiencies that should be recognized in a TELRIC environment. As AT&T cost witness Douglas Denney testified in Minnesota, LoopMod has failed to correct *any* of the

deficiencies in RLCAP the ALJ had earlier identified.[7] For instance, as described by Mr. Denney,

- LoopMod still does not use geocoded customer location data, but instead relies on distribution areas obtained from Qwest's Loop Engineering Information System ("LEIS") databases, which presumably represents Qwest's embedded/historical distribution areas;
- LoopMod continues to use the five generic distribution designs that are the same throughout Qwest's region, not specific to the state in question, and these generic designs do not consider actual customer information specific to each distribution area;
- LoopMod places distribution facilities in the same manner as RLCAP 4.0 by dedicating two or three distribution pairs per location depending on the density group, a treatment found to be unreasonable by the ALJ in the Minnesota generic UNE rate case because it creates inconsistencies between the numerator (the total increment of costs required to provide the element of concern) and denominator (the demand for the element to be provided with those facilities) of the cost-per-line calculation; and
- LoopMod maintains the same structure cost calculations that the Minnesota ALJ found "does not compute either actual or forward-looking structure costs."

37. On the other hand, the Utah PSC found that AT&T's HAI model was appropriately "forward-looking." *Id.* at 7 ("The record shows that the HAI model employs a forward-looking, economically efficient approach."). Nonetheless, the Utah PSC decided it would not rely solely on the basis of the HAI model because of concerns regarding the way in which HAI's used "proxy[s]" to determine the location of some customers. *Id.* The Utah PUC, however, did not find that by using proxy locations that the HAI model understated costs; to the contrary, it specifically rejected that claim. *See id.* at 7 ("we are not convinced by USWC testimony that the HAI model necessarily builds a deficient amount of outside plant.").

[7] *In Re Commission Investigation Of Qwest's Pricing Of Certain Unbundled Network Elements*, PUC Dockets No. P-442,421,3012/M-01-1916; *In the Matter of the Commission's Review and Investigation of Qwest's Unbundled Network Element (UNE) Prices*, PUC Docket No. P-421/CI-01-1375OAH Docket No. 12-2500-14490-, Rebuttal Testimony of Douglas Denney, p. 9 ff.

Furthermore, the Commission's Synthesis Model uses the same proxy location process for 100% of customer locations, not just those for which geocoded information is not available.

38. Thus, given the Utah PSC's express recognition that the HAI model was forward-looking and did not understate the costs of outside plant – coupled with its finding that the ICM was an "embedded" cost model – the only appropriate course would have been for the Utah PSC to set rates using HAI model. The Utah PSC, however, did not follow this straightforward approach. Instead, the Utah PSC arbitrarily set rates on the basis of the simple average of those calculated by the HAI model and US WEST's embedded ICM model. *See id.* at 7. But all this served to do was reduce somewhat the bias from using US WEST's ICM. As the Utah PSC recognized, the two models produce "significant[ly]" different "cost estimates." For example, with respect to loops, HAI generated monthly costs of $11.40 per loop while the ICM generated $21.51 per loop. *Id.* Thus, the resulting $16.46 average of the results generated by the two models is more than $5.00 per month in excess of that generated by the HAI model, which, as noted, the Utah PSC itself recognized was the only appropriately forward-looking model submitted in the proceeding.

39. The Utah PSC also used this arbitrary "split the baby" approach for switching rates. *Id.* This was clearly erroneous. Even if the HAI's method for calculating customer locations understated the necessary amount of outside plant – a conclusion rejected by the Utah PSC – that would not provide grounds for using an average of the HAI and the ICM to set non-loop UNE rates. That is particularly true given the fact that the Commission has endorsed HAI's switching cost module. *See Platform Order* 75-78 (finding that HAI "assume[s] the least cost, most-efficient and reasonable technology" use to provide switching and "generally satisif[ies] the requirement that each network function and element necessary to provide switching and

interoffice transport is associated with a particular cost"). Thus, there can be no doubt that by averaging the results of the HAI with the "embedded" ICM that the Utah PSC set switching rates in excess of TELRIC. And as explained above, federal courts have expressly concluded that this type of averaging does not result in TELRIC-based rates. *AT&T Communications of New Jersey, Inc.* v. *Bell Atlantic-New Jersey*, Civ. No. 97-5762 (KSH), slip op. (D.N.J. June 6, 2000).

40. In its 2002 Utah UNE Pricing Order, the Utah PSC set rates for several additional UNEs, such as DS1 and DS3 loops and intra-building cables that were not addressed in the 1999 Utah UNE Pricing Order. *See* Order, Docket No. 00-049-105 (Utah PSC June 11, 2002) ("*2002 Utah UNE Pricing Order*"). Again, the rates approved by the Utah PSC suffer from a number of TELRIC violations. Most notably, at the hearings AT&T demonstrated that the cost models used by Qwest for these UNEs, and accepted by the Utah PSC, did not reflect efficient costs. In particular, AT&T showed that "Qwest generally overstates its prices [by] us[ing] models [that] depend on bids from relatively small contractors with short time horizons." *2002 UNE Pricing Order* at 8. In effect, Qwest "estimated the costs of a car by using the prices it would pay for the individual parts and labor to assemble those parts, rather than the price for the car as a whole." Post Hearing Br. of AT&T and XO, Docket NO. 00-049-105, at 20 (filed Utah PSC Nov. 30, 2001). The Utah PSC agreed with this argument, *UNE Pricing Order* at 8, but made no attempt to change Qwest's costs to reflect the impact of this bias. Instead, the Utah PSC simply "encourag[ed]" the parties to develop "evidence in [the] future" to address this issue. *2002 Utah UNE Pricing Order* at 8.

V. QWEST'S WYOMING UNE LOOP RATES ARE INFLATED BY CLEAR TELRIC ERRORS.

41. On November 22, 1996, AT&T filed a petition for arbitration with the Wyoming PSC under the 1996 Act. After multiple rounds of testimony and a week of hearings, the PSC issued a 101-page order on the merits on April 23, 1997.[8] In its order, the PSC found that "the cost information which we now have before us would [not] support the acccurate determination of prices for unbundled network elements which would be consistent with 47 CFR §§ 51.505 and 51.511."[9] "Neither party has demonstrated to our satisfaction that its model fully and accurately addresses TELRIC or TSLRIC costing."[10] "U S WEST's cost study . . . utilized cost information that US WEST has allegedly submitted in Phase II [of a separate proceeding to set *retail* prices under state law], but on which the Commission has neither examined in appropriate hearings nor relied upon in any meaningful way."[11] And AT&T's cost study, "while arguably consistent with the federal guidelines, did not sufficiently recognize Wyoming's particular requirement of TSLRIC based pricing [for retail services]."[12]

42. The PSC ordered both AT&T and U S WEST to rerun their cost models with a PSC-specified cost of capital, PSC-approved current depreciation lives, and an input for income tax expense that reflect the absence of any state income tax in Wyoming. The PSC also ordered U S WEST to recover an allowance for supposedly unrecovered depreciation that US WEST had

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[8] Wyoming PSC Docket No. 70000-TF-96-319, *In the matter of the arbitration by the Public Service Commission of an interconnection agreement between U S WEST Communications, Inc., and AT&T Communications of the Mountain States, Inc., under 47 U.S.C. § 252* (order issued Apr. 23, 1997) ("1997 Arbitration Order").

[9] *Id.* at 21.

[10] *Id.* at 22.

[11] *Id.* at 44.

[12] *Id.*

included in its cost study.[13] The average of the revised values submitted by the parties, the PSC announced, would serve as interim rates.[14]

43. Before taking further action in the arbititration, the PSC issued a decision in a closely related case involving U S WEST's retail prices.[15] The two cases were linked by the Wyoming Telecommunications Act of 1995, which directed the PSC to reform US WEST's retail rate structure, with the ultimate requirement that all retail services would cover the TSLRIC of those services. Because the 1995 state statute required the adoption of cost-based rates, the retail price litigation raised many of the same issues that the PSC needed to resolve in the AT&T/U S WEST arbitration.[16]

44. With respect to threshold choice of cost models, the PSC found neither of the party's model fully acceptable. The PSC found that the loop cost model relied on by AT&T, an early version of the Hatfield Model, lacked sufficient granularity of data, had too many density zones (nine), and tended to load too many costs on the two lowest density zones. The Hatfield Model, however, was a "relatively open unitary model."[17]

45. The PSC's discussion of U S WEST's loop cost model, the RLCAP, was scathing: the RLCAP was a virtually unverifiable black box. Moreover, its inputs and assumptions—to the extent that they could be discerned—appeared to be designed to replicate

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[13] *Id.* at 21.

[14] *Id.* at 21 and 45.

[15] Wyoming PSC Docket No. 70000-TR-96-323, *In the Matter of the Application of US West Communications, Inc. for Authority to Implement Phase II of its Proposed Wyoming Price Regulation Plan for Essential and Noncompetitive Telecommunications Services* (decision served July 21, 1997) ("Phase II Retail Decision").

[16] *See* Phase II Retail Decision ¶¶ 68-80.

the costs of U S WEST's embedded network, not the costs of an efficient forward-looking network.

> - RLCAP's cost estimates depend upon "factor databases" that are under the control of U S WEST and which do not allow for either the performance of independent cost estimates or the performance of independent sensitivity analyses of U S WEST's loop cost estimates.
>
> - RLCAP is largely a "closed" model. It is not possible to completely replicate its results because many inputs and resulting outputs are considered proprietary by U S WEST. Additionally, portions of this model (certain modules) are not available to outside parties.
>
> - We note that it uses five density zones for some calculations but that U S WEST uses a base rate area and three zones for actual pricing purposes in Wyoming—another discontinuity . . .
>
> - We have not been able to see sufficiently into RLCAP and its associated models to ascertain how they deal with data or even what their components really are. It has been shown to be a slow and relatively cumbersome group of models which appear to have developed as in-house costing tools. They resist both examination and understanding, and therefore, do not appear to be able to be tested for compliance with the various legal standards which we must apply in this case (e.g., a reasonable and nondiscriminatory pricing result in the public interest) . . . .[18]

46. Accordingly, the PSC directed the parties to submit additional runs of the competing models using inputs designated by the PSC, with the further constraint that the Hatfield Model should be run to produce outputs in only three density zones.[19]

47. The PSC's choice of inputs for the compliance runs was a mixed bag. The PSC held that 65% of outside plant structure placement should be assumed to be "difficult" (i.e., above-average cost), a reversal of U S WEST's position in earlier litigation and other states,

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[17] *Id.* ¶ 94.

[18] *Id.* ¶¶ 84, 87-88, 93.

[19] *Id.* ¶ 100.

because US WEST's *embedded* cost data assertedly supported such a result.[20] Despite finding that "structure sharing will increase as telecommunications markets are opened up to competition and companies are forced to capitalize on cost saving opportunities in order to be competitive in this new business environment," the PSC assumed that only 25 percent of the cost of placing outside plant would be borne by other utilities.[21]

48. With respect to common overhead costs, the PSC rejected the 10.4 percent overhead cost factor proposed by AT&T on the theory that it "reflects too closely the level of cost that might be experienced in a truly competitive business environment"—i.e., was too TELRIC compliant.[22] Instead, the PSC split the baby by adopting a value of 15 percent—the average of the 10.4 percent factor proposed by AT&T and the lower end of the 20-25 percent range proposed by Qwest.[23] And the PSC explicitly split the baby in adopting a drop length of 90 feet, the "average of US WEST's stated [embedded] system average and AT&T's long urban drop length."[24]

49. On the other hand, the PSC rejected U S WEST's proposed cost of capital of 10.87 percent in favor of a value of 10.05 percent.[25] The PSC rejected U S WEST's proposal to adopt depreciation lives shorter than those previously prescribed by the PSC.[26] The PSC adopted

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[20] *Id.* ¶ 108.

[21] *Id.* ¶¶ 127-132.

[22] *Id.* ¶ 135.

[23] *Id.* ¶ 136.

[24] *Id.* ¶ 145.

[25] *Id.* ¶ 122-126.

[26] *Id.* ¶ 156-71.

an "objective" distribution fill factor of 75 percent.[27] And the PSC declined to approve the increases in nonrecurring charges proposed by Qwest.[28]

50. Wyoming law, however, has a peculiar feature: U S West has the right to reject PSC rate decisions that establish rates differing significantly from those proposed by the carrier. Wyoming Stat. § 37-15-203(b). U S West exercised this authority by rejecting the PSC's rate case decision in its entirety.

51. The derailment of the PSC's retail rate proceeding brought the pending UNE arbitration to a halt as well. After April 1997, the PSC issued no further decision on the merits of the unresolved cost and pricing issues for nearly two years. Instead, the PSC temporized, requesting additional rounds of evidence and holding additional hearings. The problem, the PSC announced in a letter-order to AT&T and U S WEST, was that the Commission had "determined that there should be basic 'symmetry' between the relevant wholesale prices set in arbitration and retail prices set in the U S WEST price plan case" (i.e., the then-pending retail price case).[29]

52. The PSC eventually issued a further decision on the merits on March 22, 1999.[30] In that decision, the PSC's retreat became a rout.

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[27] *Id.* ¶¶ 137-142.

[28] *Id.* ¶¶ 172-78.

[29] Wyoming PSC Docket No. 70000-TF-96-319 and 72000-TF-96-95, Letter Order dated Aug. 5, 1998 at ¶ 3.

[30] Wyoming PSC Docket No. 72000-TF-96-95 and 70000-TF-96-319, *In the Matter of the Interconnection Contract Negotiations Between AT&T Communications of the Mountain States, Inc. and U S West Communications, Inc. Pursuant to 47 U.S.C. Section 252*, Order on Rehearing (issued March 22, 1999).

53. First, the PSC declined to adopt geographically deaveraged rates in the sense contemplated by 47 C.F.R. § 51.507(f)—i.e., deaveraging to reflect the density-based cost differences of urban, suburban and rural wire centers. Instead, the PSC adopted Qwest's rate structure, which divided rates into four concentric rate zones around each central office. The latter rate structure, by the PSC's own admission, was designed to protect Qwest's existing *retail* rate structure from competitive arbitrage, while ignoring most cost differences *between* wire centers.[31]

54. The PSC's adoption of Qwest's rate structure in turn determined the PSC's choice of cost models. "We must adopt US WEST's RLCAP model," the PSC held, because it accommodates "internal U S WEST data" and because it generates outputs in a format that translates directly into U S WEST's deaveraging scheme.[32] The PSC made no mention of its previous findings that the RLCAP was an unverifiable black box, and offered no response to the evidence offered by AT&T during the 1997-99 proceedings that improvements to the Hatfield Model had eliminated the PSC's prior concerns over its granularity and accuracy.[33]

55. AT&T petitioned for rehearing of the March 1999 decision on April 21, 1999.[34] In its petition, AT&T noted that the PSC had never responded to the AT&T cost testimony showing that the RLCAP replicated the costs Qwest's embedded network, rather than the costs of a forward-looking network.[35] AT&T also reminded the PSC that it had never disavowed its

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[31] *Id.* ¶¶ 128, 131, 136, 157.

[32] *Id.* ¶ 157.

[33] *Cf. id.* ¶ 136.

[34] Wyoming PSC Docket Nos. 70000-TF-96-319 and 72000-TF-96-95, AT&T Petition for Rehearing of Commission's March 22, 1999 Order.

[35] *Id.* at 7 (citing record).

June 1997 findings in the retail rate case concerning the unverifiability of the RLCAP inputs, and the apparent inconsistency between the model assumptions and the forward-looking assumptions of the TELRIC and TSLRIC standard.[36]

56. AT&T also sought rehearing of the PSC's approval of Qwest's "deaveraging" scheme. AT&T reiterated that Qwest's concentric rate structure ignored the density-based cost differences among wire centers, adding that even the Qwest witness who sponsored the rate design "testified that he had no idea how the structure of the zones was determined."[37]

57. The PSC responded with a further decision on June 30, 1999.[38] Acknowledging "the great reliance" of the Qwest cost models on "actual" costs, "U S WEST-specific data," "state-specific factors" and "'real world' checks" – *i.e.*, embedded assumptions—the PSC nonetheless insisted that the models "use forward-looking technology."[39]

58. On July 31, 2001, Qwest initiated a generic rate proceeding to permanent establish UNE prices for all CLECs in Wyoming.[40] In the aftermath of the costly and unproductive arbitration proceeding, only two CLECs intervened (AT&T and Contact Communications); AT&T subsequently withdrew without filing testimony. On June 19, 2002,

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[36] *Id.* at 7-8 (citing July 1997 PSC decision).

[37] *Id.* at 11 (citing record).

[38] Docket Nos. 70000-TF-96-319 and 72000-TF-96-95, Order on Petitions for Reharing of U S WEST Communications, Inc. and AT&T Communications of the Mountain States, Inc., and Amending Previous Orders (issued June 30, 1999).

[39] *Id.* ¶ 15e.

[40] Wyoming PSC Docket No. 700000-TA-01-700, *In the Matter of Qwest Corporation's Request to Open an Unbundled Network Elements TELRIC Cost Docket.*

Qwest settled the case by stipulation with Contact and the Consumer Advocate Staff of the PSC.[41]

59. Even Qwest evidently recognized that its Wyoming rates would not pass muster at this Commission. On July 1, 2002 – just before filing its Section 271 Application—Qwest unilaterally reduced certain of its rates for local switching usage, local switch ports, shared transport, and tandem switching. *See* Thompson Wyoming Pricing Decl. ¶ 12. Qwest claims that these eleventh hour rate reductions produce TELRIC-compliant rates because: (1) the new rates are lower than the rates adopted by the Wyoming PSC and (2) the new rates pass the Commission's benchmarking analysis, using Colorado as the benchmark state.

VI. QWEST'S MONTANA UNE LOOP RATES ARE INFLATED BY CLEAR TELRIC ERRORS.

60. Qwest's recurring and nonrecurring prices for UNEs and interconnection in Montana are the legacy of three sets of rate proceedings: the 1996-2000 arbitration litigation between Qwest's predecessor, U S WEST, and AT&T; the 2000-01 UNE case between Qwest and five small interveners; and the "benchmarked" rate adjustments that Qwest filed on the eve of its 271 application. None of the three sets of rate changes have produced TELRIC-compliant rates. Indeed, the PSC has disclaimed any finding of TELRIC compliance, acknowledging that the issue remains to be resolved in a future proceeding.

61. The issue of UNE prices under the 1996 Act first reached the Montana PSC in the 1996-98 arbitration between AT&T and U S WEST. AT&T initiated the proceeding by

[41] Wyoming PSC Docket No. 700000-TA-01-700, Stipulation and Agreement (June 19, 2002); Wyoming PSC Docket No. 70000-TA-00-599, *In the Matter of the Application of Quest Corp. Regarding Relief under Section 271 of the Federal Telecommunications Act of 1996, Wyoming's*

petitioning the PSC for arbitration on November 22, 1996. The PSC issued its decision in the arbitration four months later. Docket No. D96.11.2000, *Petition of AT&T Communications of the Mountain States, Inc. Pursuant to 47 U.S.C. § 252(b) for Arbitration of Rates, Terms and Conditions of Interconnection With U S WEST Communications, Inc.*, Order No. 5961b (March 20, 1997) ("*Montana Arbitration Order*").

62. In its decision, the Montana PSC adopted loop prices based on the cost model submitted by AT&T, the Hatfield Model, with certain upward adjustments proposed by U S WEST. The result was a total statewide average loop price of $27.41. *Id.* at 87. The PSC adopted AT&T's proposed prices for the NID, port, local switching, tandem switching, transport, signaling links, signaling transfer points, service control points/databases, collocation, and local service provider change charge. *Id.* at 86-87. For collocation, the PSC adopted the rates proposed by U S WEST. *Id.* at 87.

63. In setting these rates, the PSC made no finding that they complied with the 1996 Act or with the TELRIC standard. The Commission found that major discovery disputes between AT&T and Qwest remained unresolved too long into the proceeding to leave sufficient time for the development of an adequate record and decision. Failure to complete discovery sooner, the PSC stated, "not only made it difficult for the other party to frame its arguments and make its case, [and] made Commission decisions on permanent prices for services and network elements not merely impractical but a virtual impossibility." *Montana Arbitration Order* at 5

Participation in a Multi-State Section 271 Process, And Approval of Its Statement of Generally Available Terms, Order on SGAT Compliance (July 9, 2002) at 2.

¶ 10.[42] Further, the PSC added, "due to the complexity of the [UNE cost] studies and the short time in which to arbitrate, it is impossible to conduct a thorough review of each of the studies." *Id.* at 81. Because of the "little time within which to complete the proceeding and render a final decision" on the "multitudinous issues and subissues" in the case, the "only practical method" of resolving that case was to "establish interim rates" only. *Id.* at 7 ¶ 15. The PSC promised to establish permanent rates "in a separate generic U S WEST costing and pricing docket where the parties can focus on costing and pricing issues and related policy matters." *Id.* at 81-82; *accord, id.* at 7-8 ¶ 16.

64. The PSC also declined in its March 1997 arbitration decision to prescribe rates in a geographically deaveraged form as required by 47 C.F.R. § 51.507(f). The PSC reasoned that the "FCC's geographic deaveraging requirements have been stayed by the 8th Circuit and we need not follow them." *Id.* at 83.

65. Nearly four more years passed before the PSC even attempted to cure this deficiency by issuing geographically deaveraged rates. Docket No. D99.12.2777, *Implementation of 47 C.F.R. § 51.507(f), Establishing Different Rates for Network Elements in Different Geographic Areas Within The State*, Order No. 6227b (Dec. 18, 2000). The "deaveraged" rates adopted by the PSC, however, were not deaveraged in the sense of reflecting the density-based cost differences of urban, suburban and rural wire centers. Instead, the PSC adopted a Qwest "deaveraging" scheme designed to protect Qwest's existing *retail* rate structure

[42] In a subsequent order on reconsideration, the PSC made clear that the party injured by the unresponsiveness of its adversary in discovery was not U S WEST. "US WEST provided no showing of prejudice . . . Much of the information requested [by U S WEST] related to AT&T's costs, which have not been shown to be relevant in this matter." Docket No. D96-11.20, Order No. 5961c, Order on Petitions for Reconsideration (July 9, 1997), at 3-4.

from competitive arbitrage. This rate structure divided rates into four concentric rate zones around each central office. The rate structure ignored all cost differences *between* wire centers. *Id.* at 6-8, 20. The PSC acknowledged that its action was driven primarily by a concern for "retail price stability," not cost recognition. *Id.* at 20. "There is reason to believe that Qwest's rate/revenue deaveraging proposal, although arguably related to costs, is arbitrary." *Id.*

66. While the deaveraging case was still pending, Qwest moved to increase the underlying rates. In June 2000, Qwest applied to the PSC for permission to implement changes—most of them large increases—in virtually all of its recurring and nonrecurring rates for UNEs and interconnection. Qwest based its cost studies on essentially the same cost models, including the ICM, discussed above. The PSC responded by instituting an investigation of the proposed rate changes in July 2000. Docket No. D2000.6.89, *Filing by Qwest Corporation, f/k/a U S WEST Communications, Inc. to Determine Wholesale Discounts, Prices For Unbundled Network Elements, Collocation, Line Sharing, and Related Matters.*

67. Perhaps because of the small number of local lines in the portion of Montana served by Qwest, the perceived high cost of rate litigation against Qwest, and the meager results of four years of UNE rate litigation between Qwest and AT&T, only six parties chose to intervene in the new case: Association of Communications Enterprises ("ASCENT"), Avista Communications of Montana, Inc., McLeodUSA Wireless, Inc., Montana Consumer Counsel, New Edge Networks, and Touch America, Inc.[43]

68. On June 6, 2001—six days before the scheduled beginning of trial—the three intervenors still remaining in the case (Avista, Mountana Wireless, Touch America, and the

[43] Montana PSC Docket No. 2000.6.89, Notice of Staff Action (served July 28, 2000).

Montana Consumer Counsel) threw in the towel. They agreed to a Qwest "compromise" proposal that increased the "interim" state-wide average loop rate of $27.41, already among the highest in the United States, to $28.37. They agreed to make permanent the non-density based method of geographic "deaveraging" that Qwest had devised to protect its existing retail rate structure from competition. And they agreed to rates for switching and other UNEs based on Qwest's cost studies. *See* Docket No. D2000.6.89, Stipulation filed June 6, 2001; *id.*, Final Order on Stipulation (served Oct. 12, 2001).

69. There was no pretense that the stipulated rates represented any principled effort to comply with the TELRIC standard. To the contrary, the stipulation contained the express disclaimer that "[n]o party's position in this docket is accepted by the other parties by virtue of their entry into this Stipulation, nor does it indicate their acceptance, agreement or concession to any rate-making principle, cost of service determination, or pricing principle embodied, or arguably embodied, in this Stipulation." Stipulation ¶ 3.

70. The Montana PSC, while ratifying the stipulation, made no findings that the stipulated rates were TELRIC compliant. The PSC expressly reserved the right to argue, in its recommendation to the FCC after Qwest's anticipated 271 filing, that "elements of the Stipulation should be changed before the FCC approves Qwest's 271 petition for interLATA market entry in the State of Montana." Docket No. D2000.6.89, Final Order on Stipulation ¶ 9. The PSC elaborated (*id.*, ¶¶ 10-11):

> 10. The Commission conditions its approval because this docket is related to Docket No. D2000.5.70, the Qwest Montana section 271 proceeding. Costing and pricing issues that arise in the 271 proceeding are not necessarily resolved by this Stipulation. Qwest concurs that the Stipulation is not all-inclusive and that other costing and pricing issues will remain if the Stipulation is

> approved. . . . The Commission expects that these and other costing and pricing issues will be addressed in another costing and pricing docket. . . .
>
> 11. Prices contained in the Stipulation may be at odds with final Commission recommendations on certain issues in the 271 proceeding. The Commission cannot be more specific because its analysis and decisions in the 271 proceeding are not complete.

71. Even Qwest evidently recognized that its Montana rates would not pass muster at this Commission. On July 3, 2002—just before filing its Section 271 Application—Qwest unilaterally lowered those rates to "expedite consideration of Qwest's Section 271 application." *See* Thompson Montana Pricing Decl. ¶ 13. Qwest claims that these eleventh hour rate reductions produce TELRIC-compliant rates because: (1) the new rates are lower than the rates adopted by the Montana PSC and (2) the new rates pass the Commission's benchmarking analysis, using Colorado as the benchmark state.

72. AT&T explains elsewhere why Qwest's benchmarking analysis is unsound. Here, it is sufficient to note that the Montana PSC, in allowing the new rates to take effect, expressly disclaimed any finding they were TELRIC-compliant. "The Commission has not undertaken the review contemplated by 47 U.S.C. § 252(f)(3)(B) and consequently retains authority to continue review of the SGAT under 47 U.S.C. § 252(f)(4)." Docket No. D2000.6.80, *Review of Qwest Communications' Statement of Generally Available Terms Pursuant to Section 252(f) of the Telecommunications Act of 1996*, Order No. 6425 (served July 12, 2001).

VII. CONCLUSION

73. For the foregoing reasons, the Washington, Wyoming, Utah and Montana state commission's committed numerous clear errors in adopting the non-TELRIC UNE loop rates in those states.

VERIFICATION PAGE

I declare under penalty of perjury that the foregoing Declaration is true and correct.

/s/ Dean Fassett

Dean Fassett
Executed on: July 31, 2002

VERIFICATION PAGE

I declare under penalty of perjury that the foregoing Declaration is true and correct.

/s/ Robert Mercer

Robert Mercer
Executed on: July 31, 2002